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RUEHBU/AMEMBASSY BUENOS AIRES PRIORITY 0088
RUEHCV/AMEMBASSY CARACAS PRIORITY 0402
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RUEHFR/AMEMBASSY PARIS PRIORITY 0264
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S E C R E T SECTION 01 OF 04 TEGUCIGALPA 001331

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STATE PASS AID FOR LAC/CAM
NSC FOR DAN FISK

E.O. 12958: DECL: 07/24/2031
TAGS: EPET ENRG PGOV PREL PINR HO
SUBJECT: HONDURAS: DIPPSA SALE A PDVSA FRONT? ALSO: FUEL
BID TERMS OF REFERENCE FINALLY TO BE RELEASED

REF: TEGUCIGALPA 1238 AND PREVIOUS

Classified By: AMB Charles Ford for reasons 1.4 (b) and (d)

¶1. (S) Summary: The Terms of Reference for the international fuel bid solicitation are due to be released on July 25. The TOR are expected to be "ex-tank," meaning bidders will be responsible for both importing and storing the fuel. This gives an apparent bidding advantage to companies that already own or can access such storage, including U.S. firms Esso and Texaco. Post fears, however, that the intent of this TOR might be to incline the process in favor of Honduran company DIPPSA, which also owns significant storage capacity. DIPPSA was reportedly purchased for over USD 65 million on July 21 by a Florida-based company (Caribbean Petrochemical Company) which was incorporated only one month ago with a capitalization of only USD 100. GOH Minister of Foreign Relations Milton Jimenez alleged to Ambassador that the company is a front for Venezuelan interests. The contract apparently has significant out-clauses, and the possibility remains that Post could help steer the GOH away from a Venezuelan solution. In a worse case scenario, PDVSA could become the key supplier to Honduras, while certain special interests receive lucrative payouts and the GOV uses DIPPSA's Gulf of Fonseca storage facilities to supply FSLN and FMLN municipalities in Nicaragua and El Salvador, likely with a view towards influencing Nicaraguan elections. End Summary.

¶2. (C) In a July 23 meeting with Ambassador (detailed septel), President Jose Manuel "Mel" Zelaya Rosales said the terms of reference (TOR) for the long-awaited international fuel solicitation will be released on July 25. Zelaya discounted any talk of nationalizing storage facilities (owned primarily by U.S. firms Esso and Texaco). According to Zelaya, the TOR will specify delivery "ex-tank," meaning the individual bidders will be responsible not only for delivery but also storage of the fuel. The GOH would take delivery on the distribution side ("at the rack") of the storage tanks -- hence "ex-tank." The TOR will be published to the Presidency website (www.presidencia.gob.hn), he said, and a public comment period of 10 days will be honored.

¶3. (S) On the surface this appears a major step forward, away from a PetroCaribe (government to government) solution and towards a market-driven and transparent outcome. Further, it appears to de-escalate the rhetoric of nationalization of the existing storage facilities and, given the "ex-tank" provision, would even seem to favor current U.S. investors Esso and Texaco in the process. However, Post fears this TOR alternatively might be the endgame of an elaborate ruse intended to ensure that certain personal and political interests win the upcoming bid solicitation.

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"DIPPSA Will Be the Key."
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¶4. (S) As reported previously, many behind-the-scenes participants in the bid process (such as former President Rafael Leonardo Callejas (National Party) and French-Argentinean dealmaker Adrian Recca) have always considered Honduran gasoline retailer DIPPSA to be the key to a winning bid strategy. Despite the GOH decision to nationalize imports and launch a bid solicitation, it has long been clear that the obstacle to executing that plan would be storage. Facing the capricious removal of their import licenses, neither Esso nor Texaco were likely to reach agreement with the GOH on use of their storage facilities. This left the GOH with only three options: build new GOH-owned facilities; nationalize the existing facilities; or use DIPPSA's facilities. Regarding the first: the GOH might still build its own facilities, but that could take up to a year. On the second: Post has fought unflaggingly to dissuade the GOH from a strategy of confiscation of the



existing assets. Despite Post's strong message, both President Zelaya and his consultant on the bid project had until recently continued to threaten such confiscation if necessary. Suddenly, on July 23, both the GOH message and tone appeared to shift dramatically.

¶5. (S) The cause of this shift in tone from casual menace to magnanimity towards the oil companies is, in Post's view, the result of the recent sale of DIPPSA, thereby making the third option viable. In a stunning confirmation of what Post had already suspected, Minister of Foreign Affairs Milton Jimenez told Ambassador that the company that purchased DIPPSA -- Caribbean Petrochemical Company -- "is a front for the Venezuelans." Assuming this is true (Post assesses that it is), and taking into account the decision to base the TOR on "ex-tank" delivery terms, the company that owns DIPPSA is now perhaps the best-positioned to win the upcoming international fuel solicitation.

¶6. Post has up to now managed to discourage a potential PDVSA bid, pointing out that PetroCaribe-inspired financing plans cannot be used to lower the pump price. Moreover, the GOH has agreed (per Post urging) to a ten day public comment period after the TOR are released. However, in the worst case scenario, the GOH might have attained precisely what was intended all along: PDVSA could become the key supplier to Honduras; certain special interests (including Recca and Callejas, who appears to be continuing his questionable role of dealmaker, but possibly members of the Zelaya administration as well) could receive lucrative payouts; and the GOV could be able to use DIPPSA's Gulf of Fonseca storage facilities to supply FSLN and FMLN municipalities in Nicaragua and El Salvador, likely with a view towards influencing Nicaraguan elections.

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Who is Caribbean Petrochemical Company?
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¶7. (S) Post has suspected from first contact that Caribbean Petrochemical Company (CPC) was a front company for other

interests, the most likely being Venezuela. The company approached DIPPSA owner Henry Arevalo unsolicited, and within two days had tabled an offer to purchase the firm -- despite the fact they had done no due diligence and that they have no experience in the downstream petroleum sector. In EconChief's talks with company representatives it soon became clear that the company also lacked even the most rudimentary understanding of political or economic conditions in Honduras, including recent GOH decisions to nationalize fuel imports. Such flagrant disregard for country risk could only be explained if an unseen local partner were actually directing CPC actions. It now appears that local partner could be Adrian Recca, finally successful in his long quest (reported extensively reftels) to structure a deal that would give PDVSA access to the Honduran market.

¶8. (S) It is unclear to Post whether CPC's actions in this regard would violate any U.S. or Honduran laws. CPC was incorporated in Florida on June 13, 2006, with a capitalization of 10,000 shares with a par value of USD 0.01 each (implying a total capitalization of USD 100). Yet somehow this firm, only one month later, was able to offer over USD 65 million for DIPPSA. (A note on the sales price: CPC told Post the sale price was USD 65 million. DIPPSA owner Arevalo told EconChief the price was USD 75 million; while President Zelaya told Ambassador the price was USD 90 million.) In a move that may have been intended to imply GOH innocence to Ambassador, Zelaya ordered FM Jimenez to investigate CPC, and made a phone call in front of Ambassador to tax authority (DEI) Director Armando Sarmiento, exhorting him to likewise investigate the firm. Esso, a 50 percent partner with DIPPSA in the Gulf of Fonseca storage facilities at Port Henecan, previously known as PetroSur, knew nothing



about the sale beyond a local press report, and told Post that when questioned on July 22, Henry Arevalo denied to Esso that the sale had happened. On that same day Arevalo confirmed the sale to EconChief.

¶9. While the existence of a contract between CPC and DIPPSA was confirmed by both companies, there appear to be significant caveats attached. On July 21 the President of CPC confirmed the contract to EconOff, but indicated that three provisions need to be met: 1) that CPC can continue to import their own fuel (Comment: Not allowable under proposed TOR. End Comment); 2) that there will be no revision in the GOH,s price setting formula (Comment: The inefficient formula gives DIPPSA solid margins on downstream operations, and will most likely be the next target of revision. End Comment); and 3) the current GOH subsidy situation will end soon (Comment: This has been threatened, but would result in a politically explosive USD 1.28 dollar per gallon increase in the pump price of gasoline. End Comment). Per the CPC President, Arevalo was in the process of obtaining a letter agreeing to these terms and conditions from President of the Congress Roberto Micheletti. Similarly, on July 25 Arevalo confirmed to EconChief that a contract has been signed, but stressed that the contract was subject to due diligence investigations and verification of the buyer's bona fides.

¶10. (S) It seems credible to Post that CPC is representing the interests of other parties, possibly PDVSA, as alleged by FM Jimenez. Post has requested (via email) that Washington-based agencies undertake basic fact-finding in an effort to establish the company's bona fides, and to determine whether any U.S. regulations or laws (for example, money laundering) have been broken in this transaction.

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Comment
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¶11. (S) Comment: In principle the current bid structure opens the way for a transparent bid process and a winner based on merit (which winner will then be responsible for

supplying or entering into a commercial agreement for storage facilities). That is the rosiest scenario, but seems unlikely to Post. The worst case scenario, as noted above, is that the terms, by requiring ex-tank delivery, discourage a number of bidders from participating while rendering other bids less competitive, thus clearing the way for the GOH to award the contract to PDVSA (via its alleged front CPC, via its front DIPPSA).

¶12. (S) Comment continued: Should both of those possibilities fail, Zelaya has said he would vacate the bid until new storage facilities could be constructed. This would certainly infuriate certain civic groups, who would be faced with the prospect of waiting at least 8 months for the bid process they are convinced (probably incorrectly) will lower pump prices significantly. Focusing on storage as the obstacle, these groups are likely to vilify the storage owners (Texaco and Esso) and might call increasingly shrilly for expropriation of those assets to allow the bid to go forward. It is worth recalling that, during the one-day taxi strike last spring, protesters blocked key highways from dawn until being broken up by police at 1400 hours local. Asked why he waited so long to act, Zelaya told Ambassador that by waiting he allowed the wrath of the public to build, and their frustrations to turn them against the taxi drivers, such that the police action, when it finally came, was seen as a relief rather than an act of state oppression. Post could foresee Zelaya using similar tactics to justify an expropriation of the storage tanks, should that prove necessary in his view. End Comment.

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